

Agence Française de Développement (AFD) Letter to Management

Executive Summary

A team comprising Camilla Bengtsson of Sida, Roland Siller of KfW, and Brigit Helms and Eric Duflos of CGAP conducted a Donor Peer Review of AFD in Paris from 10-14 March, 2003. The review is part of a 17-agency initiative launched by Development Ministers, Heads of Agencies and CGAP to concretely tackle aid effectiveness by using microfinance as a test case.

The Peer Review team focused on the internal procedures, practices and processes of AFD to identify the success factors and constraints that influence the effectiveness of the agency's microfinance operations. The Department for Finance and Private Sector (TFP) provided the team with an orientation to AFD and organized meetings with 60 people, including extensive consultation with field-level staff and partners. The team briefed Director General Jean Michel Severino, several department heads and staff on its initial findings on March 14th.

The Peer Review team found its visit to be timely given the recent reorganization and management reforms at AFD. The team hopes that this management letter will enrich the internal discussions and provide specific ideas of how AFD can build on its experience and become an international reference in microfinance.

This letter outlines AFD's strengths and challenges, and presents a number of specific recommendations for change. A matrix at the end of the letter provides a summary of the key findings and recommendations. The Peer Review Team suggests six key recommendations to enable AFD to improve the effectiveness of its microfinance interventions:

1. **Clarify the role of Microfinance at AFD.** Management should re-affirm support to microfinance and explain its crucial role for financial sector development.
2. **Operationalize and refine the financial sector strategy.** AFD should disseminate the strategy through its implementation and transform it into a living document.
3. **Further adapt the role of IFI ("Ingenierie Financiere").** The microfinance staff should be more field oriented, IFI should increase cross fertilization among its team members, include a rural finance expert, and leverage available AFD and external resources.
4. **Capitalize on existing expertise and knowledge.** AFD should create a network of internal specialists and adapt dissemination of knowledge and expertise to the needs of its field offices. It should capitalize on its experience in rural finance, and widely share it.
5. **Optimize the use and efficiency of funding instruments.** AFD should use several instruments in a sector-based approach, adapt their size and content to recipient institutions, and look for cost sharing partners.
6. **Improve portfolio quality and management.** AFD should improve the quality of its operations by developing performance-based contracts and indicators.

Background

Early in 2002, Development Ministers, Heads of Agencies and CGAP launched an initiative to improve aid effectiveness, using microfinance as a test case. As a first step in this initiative, 17 bilateral and multilateral development assistance agencies have volunteered to participate in a series of Donor Peer Reviews. These Peer Reviews are not evaluations or detailed portfolio reviews, but rather focus on each agency's internal procedures, processes, practices and systems to identify success factors and constraints to good practices in microfinance.

The short but intensive reviews result in concrete recommendations for each agency and should lead to senior management commitment to specific changes that improve the effectiveness of microfinance operations. It is also expected that the analysis and recommendations may also apply to other areas of development assistance pursued by each agency.

A Peer Review team including Camilla Bengtsson, Microfinance Advisor, Swedish International Development Cooperation Agency and Roland Siller, Senior Expert, Financial Sector Development, KfW, Brigit Helms, Lead Microfinance Specialist and Eric Duflos, Microfinance Specialist of the Consultative Group to Assist the Poor CGAP, visited AFD headquarters from 10–14 March, 2003. The review team interviewed close to 60 people from the following departments: DGL, DOE (TFP, TEN, TDH, GOA, GOB, GOC, GOE, PROPARCO), DOO, DS (EVA, SPS, POL, CEFEB), SG (DSF, DDR, ESR, AJO, DEE, DRH). Given AFD's extensive field presence, the team obtained views from country offices through telephone interviews (Mali, Senegal, Guinea, Cameroon, Mozambique, RSA, Madagascar and Cambodia). The peer review team also interviewed staff from the MAE (DCT/AP), from the groupe CERISE (CIDR/GRET/IRAM) and from ACEP and Horus Banque et Finance.

Follow-up to the Peer Reviews is envisioned both at the agency-specific level and across all agencies participating in the exercise. The review team and CGAP are available to discuss the recommendations contained in this letter in more detail and to support their implementation. The team's findings for AFD will also be combined with those from other agencies reviewed in a synthesis report. A synthesis report already exists for agencies reviewed in 2002. Overall results and issues for agencies to tackle jointly will be discussed in various fora involving technical staff and senior management. A final meeting of Ministers and heads of agencies participating in the Peer Reviews will be organized upon completion of all the reviews in late 2003/ early 2004 to share experiences and reforms made as a result of the exercise.

This management letter outlines AFD's strengths and challenges with respect to applying good practices in microfinance. It then presents a number of specific recommendations for change. Finally, a summary matrix presents the key findings and recommendations according to six analytical areas.

AFD Organizational Culture

The peer review occurred in the context of an **AFD in transition**. The challenge of adapting AFD’s traditional organizational culture to new reforms provides the background for the agency’s work in all sectors, including microfinance.

Culture	New AFD
<ul style="list-style-type: none"> • Field-oriented • Flexible approach • Intellectual / analytical • Self-reliant • Personal networks • Mobility • Experimentation 	<ul style="list-style-type: none"> • Strategy-led • Structure • Specialization / division of tasks • Larger projects • Selectivity / risk management • Visibility • Accountability

Historically, AFD culture has emphasized field experience, flexibility, responsiveness, and appreciation of intellectual debates. AFD values its ability to launch new operations quickly, and experiment with different approaches. It has traditionally looked inward and relied on personal contacts within the agency, rather than tapping external consultants or other outside expertise for technical support.

Today, this culture is confronted with a set of reforms that impose more structure on the agency. These reforms include strategy-based management, a new matrix organization, and increased staff specialization. The reforms favor large projects, higher selectivity in sectors of intervention, lower risk taking, more visibility for AFD, and accountability via results-based management systems.

This new approach creates potential conflicts that parallel a larger challenge of clarifying AFD’s identity as a development agency versus a bank. The remainder of this management letter illustrates how this dilemma is reflected in the specific context of microfinance.

AFD Strengths

AFD has a long and rich experience in microfinance, especially in pioneering new approaches in savings mobilization and rural finance. These are both areas of intense interest within the donor community, and also comprise crucial elements of an emerging international vision of financial services for the poor. At the same time, AFD's new organization and strategy is fully aligned with accepted and emerging good practices. The combination of these two factors – AFD's past experience and new strategy – provides AFD with the potential to become an international benchmark in donor support to microfinance.

- AFD has included microfinance and savings mobilization as **strategic priorities** for 2002-2006 (Plan d'Orientation Strategique). Microfinance is considered within the framework of financial sector development. Moreover, the staff demonstrates a widespread understanding that permanent access to financial services is a key goal for intervention. This strategic positioning and staff consciousness are in line with internationally accepted concepts of microfinance good practice.
- Following the recent re-organization, AFD has established a **specialized technical department** for financial sector and SME development (IFI), which will directly supervise all microfinance interventions. This new structure consolidates all AFD microfinance operations in one unit, helping to ensure sound practices are brought to bear on all AFD financial services interventions.
- **IFI's sector strategy** (CIS) includes a significant microfinance section that is consistent with international best practice. For example, it focuses on building institutions that show a potential to provide permanent access to financial services for the poor. The strategy contains a comprehensive portfolio analysis that can help inform future interventions.
- AFD has accumulated a rich **experience in rural finance and savings**. AFD has encountered both success and failure in pioneering these activities. Lessons from these experiences can feed into future operations and help fuel international debates.
- Many people have some **expertise** in microfinance at headquarters, the field offices and CEFEB. Experience has shown that there is a strong correlation between high technical capacity of staff and successful microfinance operations. This expertise could significantly contribute to bringing AFD to a position of leadership in pro-poor finance.
- AFD offers a wide variety of **funding instruments** such as grants, concessional loans, guarantees, and equity participation (through PROPARCO). Different types of MFIs require a variety of funding instruments. Also, a particular institution might need different types of funding support depending on its stage of development. The variety of AFD instruments provides an advantage to serve a wide array of institutions at different stages of maturity.
- AFD recently put in place a **portfolio rating tool** (tableau de notation qualité) to track the status of its projects, and grade them according to several parameters such as disbursement, monitoring, and scheduling. This tool provides a potential basis upon which AFD could build microfinance-specific performance tracking systems.

AFD Challenges

Notwithstanding its strengths, AFD faces a number of constraints to improving its effectiveness in microfinance.

- The liquidation of Credit Mutuel de Guinée, and the subsequent pessimistic “report of a microfinance review working group” have overshadowed AFD’s good experiences and dampened staff interest, thus bringing **uncertainty about the future of the sector**. Some staff members refer to the topic as “taboo”. Because the POS and the working group processes occurred simultaneously, staff received mixed messages about the importance of microfinance to AFD.
- AFD’s current income structure leads it to focus on **large projects**. This approach could reduce the scope of effective interventions in microfinance. As with many other areas of the private sector, some of the activities that add the most value have small grant budgets, and are often labor-intensive. International good practices have shown that grants for technical assistance and institutional capacity building are critical to expanding access of financial services to poor people.
- The POS emphasis on **selecting fewer sectors** of intervention in each country will likely result in the absence of the financial sector in most CIPs (“Cadre d’Intervention Pays”), as financial sector development has not been a traditional sector for AFD. This lack of emphasis could significantly marginalize microfinance.
- Staff does **not share a common understanding of microfinance**. Some see it as a tool for poverty reduction, others as an input in the development of agriculture, and others as part of the banking system. The agronomists’ traditional sense of experimentation and social engineering sometimes clashes with the bankers’ risk minimizing approach. These widely differing approaches result in the uneven application of good practices in operations.
- Partly because it is a new sector for AFD, and partly due to the fact that the CIS was a draft stage during the peer review, the financial sector **CIS (“Cadre d’Intervention Sectoriel”) is not yet fully mainstreamed** within AFD. The CIS does not build sufficient linkages between microfinance and other aspects of financial sector development. The CIS also underestimates the experience of AFD in rural finance and savings. This means that AFD risks losing the opportunity to build new models of rural finance by combining its experience in rural finance with the good practice spelled out in the CIS.
- **IFI’s microfinance team** needs to become more operational and demonstrate its value added, especially to the field offices. This team remains too isolated within IFI, and has insufficient resources to fulfill its multiple responsibilities (project identification, dissemination and training, portfolio performance monitoring, involvement with CIP, exchange and partnership, project restructuring and refinement of strategy).
- **Experience and expertise in financial sector** development is limited outside of TFP, partly due to the lack of opportunities to capture available internal and external knowledge, and

partly because of inadequate channels used for information sharing (too many reports and not enough training, debates, and on the job support). This gap could prevent staff from fully internalizing the new strategy.

- The **quality of the portfolio** appears to be uneven, which is the case of most donor agencies. An initial portfolio review by IFI shows a wide discrepancy in the level of quality of the projects. Portfolio knowledge needs to be interpreted with caution. AFD has not yet developed specific microfinance indicators, and cannot track performance on a systematic basis.
- Staff might be tempted to launch more **multi-sectoral projects** to fulfill the requirements for larger projects. These multi sector projects could likely include micro credit components. Such components may not receive the proper technical attention they need because they are often not visible within the larger project. In the absence of established project teams, it is unclear who would assume technical leadership on these credit components, raising concerns about quality.
- AFD's grant instruments **lack flexibility**. For example, preparation grants can only be used at the country level, and are partially controlled by the government. They are not easily used to support capacity building, sectoral studies, or cross-country/regional/global work.

Recommendations

AFD has reached a crossroads. The agency is at the forefront of integrating microfinance into the financial sector, ensuring permanent access by poor people to financial services. At the same time, AFD could leverage its existing experience and expertise in rural finance. AFD needs to make the choice of either becoming a minimal player in the sector or gaining a position of leadership in microfinance. But this choice is not free from costs and entails active commitment and investment.

The Peer Review team has specific recommendations for AFD to build on its strengths and comparative advantages to improve its effectiveness in pro-poor finance.

1) AFD should **clarify the role of microfinance** in its strategy and operations:

- *Re-affirm top management commitment.* The peer review team believes that top management should identify a high level champion who can bring microfinance back on the agenda. This champion could lead the internal microfinance network, make a declaration on microfinance at a highly visible event, or publish an article on financial sector development in a respected newspaper (e.g. Le Monde, the Financial Times). This commitment could also be declared during a staff conference or board meeting.
- *Confirm the role of microfinance within financial sector development:* An emerging consensus among international development agencies sees microfinance as an integral part of the financial sector, not a marginal activity limited to fulfilling specific and narrow needs of a

particular target group. While AFD's current structure is highly conducive to operationalizing this vision, it needs to develop a coherent statement of the role of microfinance in financial sector development. AFD should draft a two-page Operational Note and work with Department heads and field offices to devise strategies for staff to internalize the core messages. IFI ("Ingenierie Financiere") could mobilize the champion to promote the Note.

- *Identify solutions to adapt funding size to market demand:* Experience shows that small projects yield the best results in supporting financial services for the poor. These results can benefit large numbers of people on a permanent basis, if done correctly. On the other hand, large projects, for instance funding for large credit lines, can damage financial intermediaries, markets, and the ability of other donors to work in a sustainable manner. Acknowledging the requirement to move toward larger average project sizes, AFD management and technical staff will need to identify ways to launch microfinance projects with appropriate budgets and remuneration from the French government. This objective could be achieved by sharing cost with other donors through instruments like the Special Purpose Vehicles, or by cross-subsidizing microfinance operations with large projects.

2) AFD needs to operationalize and refine its **financial sector strategy**, demonstrating its full meaning and effectiveness through implementation.

- *Disseminate the strategy through its implementation in two or three countries.* While AFD has developed a first class strategy for microfinance, testing it on the ground will transform it into a reality. The peer review team suggests that IFI identifies two or three countries where AFD can make a difference in the financial sector, based on its strategic interest, comparative advantage and local demand. Country identification criteria should also include opportunities for working with other donors through co-funding. Building on the CIS and CIPs for these countries, AFD would design a program to work at different levels of the financial sector. For example, it could include projects in strengthening formal banks, promoting micro savings services diversification, supporting networks or auditors, and reinforcing the supervisory capacity of the institution responsible for ensuring the security of depositors. It would be crucial to develop appropriate indicators to track performance of each type of project and adjust the approach accordingly.
- *Build new models for rural finance:* AFD could break new ground in rural finance, especially in those countries where it has gained significant experience. While previous AFD operations had mainly been associated with rural development, the new IFI strategy puts the right emphasis on the need to launch interventions only when they lead to permanent provision of services. Microfinance interventions should not, however, be isolated from the rest of AFD's development work. Concretely, the rural development division and IFI need to further define the domains of rural development and financial sector development. Together, they could find complementarities, share experiences, and ensure compatibility between the CIS and interventions on the ground. Mali is one of the countries where AFD could test this approach.

3) AFD should maximize **IFI's effectiveness**:

- *Spend more time in the field*: The peer review team recommends that IFI's microfinance staff spend more time in the field to gain a better understanding of the relationship between financial systems and development. It would forge better relations with field-based staff, ensure that the strategy is implemented, and make expertise available to help countries identify possible sector-based interventions and/or monitor the progress of their projects.
- *Add one expert in rural finance to IFI*. Based on the comparative advantage of AFD in rural areas, and the need to build bridges between rural development and the financial sector, the peer review team believes that adding one rural finance expert will strengthen IFI. This new person would play a key role in (i) disseminating AFD lessons learnt in rural finance, (ii) re-conceptualizing rural finance in the context of the new strategy, and (iii) enabling AFD to take part more actively in sharing with the international community, as rural finance is at the top of the international agenda.
- *Increase cross fertilization within IFI*. To better reflect microfinance as part of the financial sector, the peer review team advises more integration of IFI staff to comprise a single team. All staff should look for ways to integrate microfinance within the financial sector. This approach would bring all of IFI's expertise to bear on microfinance issues and expose microfinance experts to the broader financial sector development agenda. This integration could include internal training and learning by doing.
- *Secure funding for external consultants*: AFD should consider hiring external consultants to complement the expertise of AFD. This would broaden AFD's horizon, increase the variety of ideas and methodologies and complement existing experiences. While keeping as much expertise as possible internally makes sense, the peer review team recommends that management identify a reasonable specific budget that IFI could use for strategic consultancies. This could be done internally or through co-funding with other donors.

4) AFD should **optimize existing knowledge and expertise**, both within and outside of the agency.

- *Build and animate a network of AFD specialists*: The peer review team recommends that IFI consolidates a network of all the people with expertise and interest in microfinance. This network would be composed of staff from headquarters, CEFEB, and field offices. Building the network would involve the following tasks: (i) create a microfinance resource address book; (ii) analyze training needs of the network; (iii) train the network and use it to disseminate and refine the strategy; and (iv) involve the network in the identification of key programs. Ultimately the network could train non-microfinance specialists internally.
- *Set up a helpdesk*: IFI should help spread good practices within AFD, especially among non-microfinance specialist staff. This could be done in the form of a help desk. Concrete ideas

for this service would be: cataloguing key lessons learnt from the field and sharing them through the intranet, and matching technical needs with network human resources. IFI and the help desk would need to package international expertise and material in a way that can be used by field offices. Concise demand-responsive documents should be favored over lengthy ones.

- *Open up AFD to outside influences:* In line with the POS, AFD could significantly increase its exposure to the international microfinance scene. This exposure would enable AFD to play a more significant role, increase visibility on the international scene, and integrate new ideas. Methods for enhancing AFD's international profile include participating in international microfinance forums, co-funding initiatives with other donors with complementary comparative advantages, cooperating further with international fora like CGAP, and using international consultants and operators.

5) AFD should adapt its **funding instruments** to the needs of pro-poor financial services.

- *Adapt instruments to microfinance:* The peer review team recommends that AFD more closely matches its instrument to specific circumstances and local contexts. Different types of instruments are appropriate for different types of financial institutions and different levels of maturity. For example, depending on the maturity of a financial institution, and on the nature of its financial activities, a grant might be more appropriate than a guarantee, or a concessional loan, or equity participation. AFD could also use different instruments with one institution at different stages of its development.
- *Utilize the full scope of instruments in the context of a sector approach:* AFD should experiment with using the full scope of its instruments in the 2-3 pilot countries when appropriate. For example, AFD could use grants to fund activities at the supervisory level and for product development of some promising MFIs, concessional loans for microfinance institutions that need subsidized financing, guarantees for institutions to leverage bank loans, and equity investments for the leading star.
- *Identify co-financing opportunities:* The peer review team recommends that AFD identify co-financing opportunities, to share risks, strengthen its own capacity, and complement its available instruments. AFD needs to look for partners with complementary instruments, especially small flexible grants. An obvious potential partner would be the Ministry of Foreign Affairs which has grant funding for capacity building. Another possible solution would be to find an existing donor that could delegate the management of small grants to AFD.
- *Refine the instrument:* As co-funding cannot answer all AFD needs, the team recommends that AFD refine its grant instruments, so that they can be used for funding capacity building, sectoral studies, or cross country/regional/global projects. AFD should set aside more funding outside of the country framework to fund such initiatives. This funding could take the form of a regional grant facility available for small technical assistance interventions.

6) AFD needs to improve its **portfolio quality and management**.

- *Track performance:* IFI should develop a set of specific performance indicators that enable AFD to track the quality of the microfinance portfolio. Such indicators would enhance the effectiveness of AFD microfinance operations, increase accountability for results, improve its impact, and foster lessons learned. These indicators could be included in performance-based contracts with its partners and operators. These indicators could be linked with existing reporting frameworks like the Microfinance Information Exchange (MIX).
- *Improve standards and quality control:* In cooperation with the future internal network, IFI could develop standard TORs for selection of partners, project design and evaluations that include technical standards corresponding to good practices. IFI could design a check list of key issues that need to be raised when current projects are being re-structured or new projects developed. These tools would enable staff to systematically integrate good practice standards in their microfinance operations.

AID EFFECTIVENESS AND MICROFINANCE MATRIX – Agence Française de Développement (AFD)

		Analysis	Recommendations
1.	Strategic Clarity and Organizational Culture	<ul style="list-style-type: none"> • Microfinance is considered a strategic priority in the overall AFD 2002-2006 strategy (POS) • Liquidation of Credit Mutuel de Guinee and subsequent reports have created uncertainty about MF • The vision on the purpose of MF differs throughout the organization • The new financial sector strategy (CIS) includes a microfinance section consistent with good practices • CIS is not yet mainstreamed and lacks linkages between MF and financial sector • AFD transition creates tension between traditional culture and new structure, and between banking/risk minimizing and development/risk taking mentalities • Incentives trend toward large projects and fewer sectors could marginalize MF 	<ul style="list-style-type: none"> • Identify a high level microfinance champion who can re-affirm top management commitment to MF • Confirm the role of microfinance within financial sector development and build linkages with other sectors to avoid isolation • Develop a two page note to operationalize the CIS • Build ownership on CIS, refine and disseminate it through its implementation in two or three countries • Open up to outside influences through participation in international for a • Identify solutions to reduce transactions costs and adapt funding size to market demand
2.	Technical Expertise & Resources	<ul style="list-style-type: none"> • AFD has established a specialized technical department for financial sector and SME development, which supervises MF • Expertise and experience in financial sector development is limited outside of TFP • IFI's microfinance team is not yet fully operational and field oriented • AFD has gained some experience in cross-cutting areas such as rural finance and savings and developed a good understanding of local context, but there is no formal network yet 	<ul style="list-style-type: none"> • IFI microfinance staff should spend more time in the field to prove itself by creating value added to other departments and field offices • IFI should add one rural finance expert to capitalize and expand existing AFD experiences in rural areas • Increase cross fertilization within IFI to further integrate microfinance into financial sector • Secure extra-project funding to hire external know-how
3.	Organizational Structure and Flows	<ul style="list-style-type: none"> • Technical staff has insufficient resources to fulfill its multiple tasks • There is no system or network to capture available internal and external knowledge 	<ul style="list-style-type: none"> • Build and animate a network of AFD specialists who can disseminate the strategy, capitalize experience, help in project identification, and train other staff on microfinance • Open up AFD to outside influences through co-funding and hiring international consultants & operators

			<ul style="list-style-type: none"> • Set up help-desk to spread good practice in a way that can be used by field offices
4.	Instruments and Incentives	<ul style="list-style-type: none"> • Full range of funding instruments relevant to funding microfinance operations (grants, concessional loans, guarantees and equity participation) • Grant instruments, such as preparation grants, lack flexibility and can not easily finance capacity building , sectoral studies and regional work • Staff might also be tempted to launch more multi-sector projects for which credit component might not receive appropriate attention 	<ul style="list-style-type: none"> • Match funding instruments with types of financial institutions and their level of maturity • Utilize the full scope of instruments in the context of a sector approach in 2-3 pilot countries • Seek to co-finance projects with partners that have complementary instruments (MAE and others) • Set aside funding outside of country framework for small technical assistance interventions
5.	Project Cycle	<ul style="list-style-type: none"> • The quality of portfolio seems uneven and needs to be taken with caution, since no specific indicators have yet been developed for MF • The existing portfolio rating tool provides a potential basis to build MF performance tracking system. 	<ul style="list-style-type: none"> • Track performance by developing specific MF indicators that can be linked with global reporting frameworks (such as the MIX) • Include indicators in performance based contracts with implementing partners • Improve standards and quality control by developing standard TORs and check list of technical issues which need to be raised for new project & project phase
6.	Future Microfinance Operations	<ul style="list-style-type: none"> • AFD could lose experience built in rural MF and savings-led MFIs • AFD could become a benchmark donor in microfinance 	<ul style="list-style-type: none"> • Operationalize the vision of integrating MF into financial sector development • Build new models for rural finance based on experience in rural development and financial sector approach • Allow experimentation while focusing on financial sector approach • Open up more actively to international debates and influences

Le Directeur Général

Paris, le **11 AOÛT 2003**

CGAP
c/o Banque Mondiale
66, avenue d'Iéna
75116 PARIS

A l'attention de Madame Brigit Helms

Madame,

Je vous remercie de l'envoi de la « Lettre au management » qui fait suite à la revue de l'Agence Française de Développement sur la microfinance. Je tiens à féliciter l'équipe de revue pour la qualité du travail accompli et à souligner l'intérêt que cet exercice a suscité au sein de l'AFD. La forte mobilisation à l'occasion de cette revue à tous les niveaux de l'AFD, aussi bien dans les agences qu'au siège, atteste que cette revue était opportune et importante pour l'AFD.

Les recommandations formulées par l'équipe de revue nous paraissent dans l'ensemble fondées et seront suivies dans leurs principales lignes ; certaines font déjà l'objet d'une mise en œuvre. Par domaine d'action, les orientations sur lesquelles nous nous engageons et les actions envisagées sont les suivantes :

1. Clarifier le rôle de la microfinance à l'AFD

L'engagement de l'AFD en faveur de la microfinance est inscrit comme une priorité dans notre plan d'orientation stratégique. Il a depuis été réaffirmé par la Direction générale lors de l'examen du cadre d'intervention relatif au secteur financier et au développement du secteur privé. Le choix de la microfinance comme secteur de concentration pour l'AFD a été acté à cette occasion. C'est dans cette logique que le cadre sectoriel d'intervention spécifique à la microfinance sera présenté au Conseil de surveillance de l'AFD en octobre 2003.

Le Management du Département en charge du secteur financier est décidé à porter et partager cette stratégie et l'expérience de l'AFD aussi bien en interne que dans les instances internationales. Nous envisageons de faire, à l'occasion de la réunion annuelle du CGAP à Paris en novembre 2003, une communication de l'AFD aux médias sur la microfinance. Une plaquette de présentation de l'action de l'AFD dans ce secteur sera préparée pour diffusion aux partenaires de l'AFD.

Nous partageons la vision de la microfinance comme faisant partie intégrante du secteur financier et nous diffuserons cette vision au sein de l'AFD et à travers nos projets.

J'ai noté le souci de l'équipe de revue relatif à la taille des projets. Je peux vous assurer de la volonté permanente de l'AFD de calibrer ses financements en fonction du besoin identifié de la contrepartie. C'est en ce sens qu'il a été acté que nous ferons exception à la règle de la taille minimale des projets pour ce qui concerne la microfinance.

2. Faire vivre et évoluer la stratégie relative au secteur financier

L'AFD a commencé à concrétiser sa stratégie sectorielle dans plusieurs pays.

Du fait de nos instruments et de nos moyens limités, une intervention simultanée à différents niveaux (institutionnel, IMF) se fera de manière sélective. Nous pourrions envisager une telle action dans la zone UEMOA, en concertation avec d'autres bailleurs de fonds. Au Kenya, une intervention « à plusieurs étages » est en préparation, avec une différenciation de l'action selon le niveau de structuration des institutions de microfinance qui seront appuyées.

L'AFD a la volonté de développer des indicateurs d'impact. Il est donc naturel qu'elle développe des indicateurs spécifiques à la microfinance. Cet aspect fera l'objet d'un travail au cours des prochains mois, sur lequel nous serions heureux d'avoir l'appui du CGAP.

Nous partageons avec l'équipe de revue la conviction que l'AFD doit continuer à œuvrer dans le financement rural. Toutefois, ce domaine étant à la fois plus difficile et plus risqué que le financement en milieu urbain, nous progresserons prudemment et par étape dans nos interventions rurales. Les deux départements concernés (secteur financier et développement rural) travailleront ensemble sur ce thème ; ils ont commencé à réfléchir sur le Mali, où l'AFD a une longue expérience. Le Burkina Faso pourrait également donner lieu à une telle collaboration.

3. Adapter le rôle d'IFI (la division d'ingénierie financière en charge de la microfinance)

L'AFD a augmenté son budget global de missions, de façon à améliorer le suivi de ses opérations, tout en favorisant l'identification et l'instruction de nouveaux projets. Le département en charge du secteur financier a donc un budget de mission lui permettant d'envoyer ses équipes sur le terrain à différents moments de la vie du projet. De cette manière, IFI (qui est une division nouvellement créée) approfondira sa connaissance du terrain.

La suggestion de l'équipe de revue d'inclure dans IFI un expert en finance rurale nous paraît intéressante, mais ne rentre pas dans le cadre des évolutions prévues à court terme. Elle pourrait être suivie d'effet en fonction de l'évolution de notre portefeuille. Il nous semble plus porteur qu'IFI crée rapidement et anime un réseau de spécialistes ayant des compétences dans ce secteur au sein de l'AFD, qui inclura des personnes disposant d'une expertise en finance rurale.

Nous agréons l'idée que la microfinance ne doit pas rester confinée au sein de l'équipe d'IFI. C'est ainsi que plusieurs chargés de missions de la division, dont le portefeuille de projets à l'origine n'était pas orienté sur la microfinance, travaillent d'ores et déjà sur des projets de microfinance, avec l'appui des agents plus expérimentés dans ce secteur. Ces agents bénéficieront de formations en microfinance.

L'équipe de revue recommande le développement du recours par l'AFD à des consultants. Cette question est en cours de débat en interne, dans le cadre budgétaire global de l'AFD.

4. Capitaliser l'expertise et les connaissances

Comme le recommande l'équipe de revue, l'AFD va constituer un réseau interne de toutes les personnes disposant d'une expertise en microfinance ou intéressées par ce sujet.

La création d'un « guichet de dépannage » tel que proposé par l'équipe de revue n'est pas envisageable actuellement, au vu des moyens dont dispose la division IFI. Ce rôle de dépannage continuera à être assuré par le chef de projet. Cependant le réseau permettra le lien avec l'expertise internationale et fournira un support en tant que de besoin.

Nous entendons augmenter la participation de l'AFD sur la scène internationale, et y impliquer plus que par le passé la hiérarchie de l'AFD, au niveau du responsable de division et du responsable de département.

5. Optimiser l'utilisation des instruments de financement

L'adaptation des instruments de financement de l'AFD à la microfinance et l'utilisation de la gamme complète des instruments de l'AFD dans le contexte d'une approche sectorielle sont des éléments importants de notre cadre d'intervention sectoriel dans le secteur financier (CIS).

Cette démarche est mise en application dans les projets de microfinance qui ont fait l'objet de décisions de financement fin 2002 en Afrique du Sud et au Mali et dans ceux qui sont actuellement en préparation en République Dominicaine et au Kenya.

L'identification d'opportunités de cofinancements est déjà un axe central de la stratégie globale de l'AFD, ainsi que de la stratégie relative au secteur financier. Nous poursuivrons dans cette voie. Cette démarche est notamment mise en application dans le projet en préparation au Kenya.

L'équipe de revue préconise d'améliorer la disponibilité de fonds permettant le financement d'études ou de projets sur plusieurs pays. En fonction de l'intérêt manifesté par les Etats, l'AFD est d'ores et déjà en mesure de recourir aux Fonds d'études et de préparation de projets pour des projets ayant trait au secteur de la microfinance, même si l'intervention vise des institutions non publiques (cf. au Kenya). Par ailleurs, l'AFD a, au cours des dernières années, mobilisé le Fonds d'Appui aux Interventions (FAI), ressource sur subvention mise à disposition de l'AFD, pour financer des études à caractère transversal sur la microfinance. Grâce à la mise en place de la Direction de la stratégie, l'AFD pourrait si elle le souhaitait,

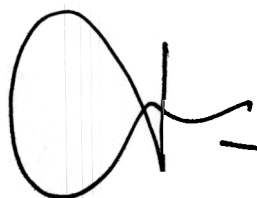
mener une réflexion transversale sur la microfinance afin d'apporter sa contribution aux débats en cours sur ce secteur.

6. Améliorer la qualité et la gestion du portefeuille

La qualité du portefeuille de projets de l'AFD est un souci permanent de l'AFD, énoncé dans le Plan d'orientation Stratégique (POS) de notre établissement. Dans ce cadre, IFI (avec l'appui du Département politique générale) développera une série d'indicateurs de performance spécifiques aux institutions de microfinance qu'elle appuie. Un premier élément d'information est disponible à travers le tableau présenté dans le cadre d'intervention sectoriel de la microfinance, qui fait apparaître le coût des projets, rapporté à un euro de crédit octroyé.

Bien entendu, l'AFD maintiendra le contact avec le CGAP pour l'informer des actions menées suite aux recommandations formulées par l'équipe de revue. A cet égard, nous remercions vivement le CGAP pour la disponibilité qu'il manifeste auprès de l'AFD.

Je vous prie d'agréer, Madame, l'assurance de mes sentiments distingués.

A handwritten signature in black ink, consisting of a large, stylized 'S' followed by a vertical line and a horizontal line extending to the right.

Jean-Michel SEVERINO

Paris, 11 August 2003

CGAP
c/o World Bank
66, avenue d'Iéna
75116 PARIS

To the attention of Ms. Brigit Helms

Dear Ms. Helms,

Thank you for the "Letter to the Management" following the microfinance peer review of the Agence Française de Développement (AFD, French development agency). I would like to congratulate the review team for the quality of its work and emphasize the interest that this exercise generated within AFD. The high degree of mobilization for this review at all levels of AFD, both in its field offices and at its headquarters, attests to the fact that this review was timely and important for AFD.

The recommendations formulated by the review team seem to be well-founded overall and their main principles will be implemented. Some of them are already being implemented. By category of activity, the actions we envisage are as follows:

1. Clarify the role of microfinance at AFD

AFD's commitment to microfinance is included as a priority in our Plan d'Orientation Stratégique (POS, strategic orientation plan). This priority has since been re-affirmed by our General Management during its examination of the intervention framework for financial sector and private sector development. The choice of microfinance as a focus sector for AFD was officially endorsed on this occasion. The microfinance-specific sector strategy will be presented to AFD's Supervisory Board in October 2003.

The Management of the Department in charge of the financial sector has decided to share this strategy and AFD's experience both within AFD and with international organizations. We plan to issue a statement to the media concerning microfinance for the CGAP's annual meeting in Paris in November 2003. A brochure presenting AFD's action in this sector will be prepared for distribution to AFD's partners.

We share the view that microfinance is an integral part of the financial sector and we will disseminate this vision inside AFD and through our projects.

I have taken note of the team's concerns regarding project size. I can assure you that AFD wishes to calibrate its funding in function of the identified needs of its partners. Accordingly, management has officially decided that we will make exceptions to the minimum project size rule when it comes to microfinance.

2. Operationalize and refine the financial sector strategy

AFD has begun to operationalize its sectoral strategy in several countries.

Due to our limited resources and instruments, simultaneous intervention on different levels (institutional, MFI) will be done in a selective manner. We could envisage such an action in the WAEMU zone, in coordination with other donors. We are currently preparing a "multi-stage" operation in Kenya, with different actions depending on the developmental stage of the microfinance institutions that we will support.

AFD is committed to develop impact indicators, and will naturally develop specific indicators for microfinance. We will complete this work during the coming months and we would be happy to receive CGAP's support.

We agree with the review team that AFD must continue to work in the field of rural finance. Nevertheless, as this field entails more challenges and risks than urban financing, we will progress step by step and with prudence in our rural interventions. The two departments concerned (financial sector and rural development) will work on this subject together; they have begun to think together of possible joint operations in Mali, where AFD has extensive experience. Burkina Faso could also give rise to such collaboration.

3. Further adapt the role of IFI (the financial engineering division in charge of microfinance)

AFD has increased its overall budget for missions to improve monitoring as well as the identification and examination of new projects. The department in charge of the financial sector has a mission budget to send its teams in the field at various times during the project cycle. IFI (which is a newly created division) will use this opportunity to deepen its knowledge of the field.

We find the review team's suggestion that a rural finance expert be included in IFI interesting but it is not part of our short term plans. We may act upon this suggestion according to the evolution of our portfolio. We feel that it would be more promising to rapidly create and animate a network of specialists with skills in this sector within AFD, which would include people with rural finance expertise.

We agree that microfinance should not remain confined within the IFI team. Thus, several of the division's project managers, whose project portfolios were not originally oriented towards microfinance, are already working on microfinance projects with the support of staff with more experience in this sector. This staff will receive training in microfinance.

The review team recommends developing use of consultants by AFD. This question is being discussed within AFD, in the framework of the AFD's overall budget.

4. Capitalize the existing experience and the knowledge

As recommended by the review team, AFD will form an internal network of all people who have expertise in microfinance or are interested in this subject.

The creation of a helpdesk as proposed by the review team cannot currently be envisaged in light of the resources available to the IFI division. Project leaders will continue to fulfill this role. However, the network will provide linkages with international expertise and provide support as needed.

We intend to increase AFD's participation in the international scene and further involve AFD's management in this area, at division manager and department manager levels.

5. Optimize the use of funding instruments

Adapting AFD's funding instruments to microfinance and using the full range of AFD instruments in the context of a sectoral approach are important elements in our financial sector strategy (CIS).

AFD is applying this approach in recently approved microfinance projects in South Africa and Mali and in those currently being prepared in the Dominican Republic and Kenya.

Identifying co-financing opportunities is already a central axis in AFD's overall strategy, as well as its financial sector strategy. We will continue in this direction. This approach is notably being applied in the project under preparation in Kenya.

The review team recommends improving the availability of funds allowing studies or projects to be funded in several countries. Depending on the interest shown by governments, AFD is already able to make use of the Fonds d'Etudes et de Préparation de Projets (study and project preparation fund) for projects involving the microfinance sector, even when the operation targets non-public institutions (*cf.* in Kenya). In addition, AFD has in recent years mobilized the Fonds d'Appui aux Interventions (FAI, intervention support fund), a subsidy-based resource made available to the AFD, to finance crosscutting studies on microfinance. Thanks to the creation of the Strategy Department, AFD could also conduct crosscutting research on microfinance to contribute to current debates on this sector.

6. Improve portfolio quality and management

AFD's portfolio quality is of constant concern for AFD and is highlighted in our institution's Plan d'Orientation Stratégique (POS, strategic orientation plan). In this framework, IFI (with support from the General Policy Department) will develop a series of performance indicators specifically designed for the microfinance institutions that it supports. Initial ideas are available in the table presented in the sectoral strategy for microfinance, which shows project cost per euro lent.

Of course, AFD will remain in contact with CGAP and keep it informed of the actions undertaken following the recommendations of the review team. In this regard, we sincerely thank CGAP for its availability to support AFD.

Yours sincerely,

Jean-Michel SEVERINO